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E.O. 12958: DECL: 10/05/2018
TAGS: EFIN ECON ETRD BEXP ET
SUBJECT: ETHIOPIA SEEKING IMF FACILITY TO STEM FOREX CRISIS

REF: ADDIS 2569

Classified By: Charge d'Affaires, a.i. Deborah R. Malac for reasons 1.4 (b) and (d).

SUMMARY

¶1. (SBU) The Ethiopian Government (GoE) has decided to approach the International Monetary Fund (IMF) for an emergency balance of payments loan facility to mitigate the country's foreign exchange crisis (reftel). The loan would be Ethiopia's first formal arrangement with the IMF in years. With hard currency reserves consistently below the level of six-weeks of imports over the past five months, the USD$200 million facility will return foreign exchange (forex) levels to a more comfortable margin over the short term. Still, the GoE is unwilling to consider liberalizing its rigid foreign exchange regime and its only medium-term strategy to address what government officials acknowledge to be a structural problem is to attract foreign investment and promote exports. Despite the IMF loan and a couple of commercial hard currency loans to state owned enterprises which will reduce some demand for hard currency, American firms seeking to sell products in Ethiopia will continue to face challenges in the Ethiopian market for the foreseeable future. Post strongly supports the IMF loan as a means to address the immediate forex crisis as well as to open the GoE to a much more direct dialogue with the IMF to address the existing structural problem. End Summary.

¶2. (SBU) Charge and Pol/Econ Chief met with Trade and Industry Minister Girma Birru on October 3 and with Economic Advisor to the Prime Minister Neway Kiristos Gebreab on October 6 to express USG concern about Ethiopia's forex crisis and its impacts on American firms seeking to do business in Ethiopia.

STRATEGIES TO ADDRESS THE FOREX CRISIS

¶3. (SBU) Charge and Pol/Econ Chief expressed great concern that Ethiopia's forex crisis is becoming untenable, is negatively impacting U.S. businesses seeking to trade with

Ethiopia, and risks future growth. After five months in which reserves have not exceeded the equivalent of six weeks of imports, Minister Girma admitted that "we do not know how to address this in the short term." Arguing that the balance of payments crisis stems from Ethiopia's rapid growth, Girma told Charge that the GoE's only strategy to address this was by expanding exports and attracting foreign investment. Girma conceded that neither of these approaches would provide a near term solution and, even if current figures doubled, neither would be adequate to balance supply and demand for hard currency even in the medium term. Both Minister Girma and Ato Neway noted that commercial loans sought by the state-owned Ethiopian Electricity Production Company (EEPCO) would provide a bit of reprieve as these would allow EEPCO -- currently finalizing several huge, import-dependent hydroelectric dams -- to stop competing for hard currency from the same limited pot as all other businesses in Ethiopia. (Note: Minister Girma referred to a large loan from JP Morgan and Ato Neway referred to a loan from Morgan Stanley. It is not clear if these are two separate loans or if one the officials simply got his Morgan's confused. End Note.) Still, Girma acknowledged that the global financial crisis has put these loans on hold, thus, further delaying relief.

¶4. (SBU) Minister Girma noted that as the GoE struggles to maintain a minimum reserve level, the little remaining forex must be rationed. Girma was forceful in noting the GoE's opposition to the administration directing who should/should not get forex. He noted that the GoE would most prefer soft loans of hard currency or the establishment of a credit

scheme through which Ethiopia could purchase oil on the world market. A six-month credit for oil would provide a dramatic improvement to the country's cash flow challenge, but as the rest of the world pays cash for oil, and Ethiopia does not have a precedent of receiving an import credit for oil, Girma recognized that such a credit is unlikely.

¶5. (SBU) Pol/Econ Chief inquired whether the GoE would consider permitting franco valuta importation during this lean period. Girma noted that the GoE had allowed franco valuta cement imports earlier this year -- on his strong recommendation -- but conceded that that experience only demonstrated that such a franco valuta scheme merely delays the demand for hard currency once repayment of the outside-secured forex comes due. Further, Girma noted that if such repayment comes due when forex reserves remain limited, importers simply go to the black market to obtain forex, further depreciating the exchange rate and fueling inflation. Of course, if companies have their own hard currency stocks, both officials highlighted, there is no impediment to them using their own forex reserves to pay for imports. Ato Neway noted that companies importing inputs required to produce exports that will earn hard currency do receive preferential access to forex, but those companies that need forex to import items such as consumer goods for domestic sales will simply have to "suck it up."

BROTHER CAN YOU SPARE $200 MILLION?

¶6. (SBU) Opposed to the intrusive nature of the IMF when engaged in formal agreements, the GoE has long opposed having another formal relationship with the Fund. Instead, for the past several years the GoE has permitted an IMF resident office in Ethiopia and annual Article IV consultations, which allow for an economic policy dialogue but do not guarantee the IMF open access to government economic information or the option to impose conditions of policy shifts for subsequent tranches of funds. In a surprising shift, however, Minister Girma disclosed that the GoE is now approaching the IMF for a USD$200 million balance of payments facility designed to assist countries to deal with the global oil price shock. According to Girma, the loan would come in an initial USD$50

million tranche with additional tranches coming later. Ato Neway reported that, while the GoE would like to get "as much as we can" from the IMF loan, the current request is actually the maximum level available from this particular IMF facility.

¶7. (U) Minister Girma noted that in initial discussions with the IMF, Fund officials expressed skepticism about giving a loan under a facility linked to the global oil price shock when the GoE continues to subsidize domestic fuel sales significantly. According to media reports, two hours after our meeting with Minister Girma, the Council of Ministers approved a five percent domestic fuel price increase and granted the Ministry of Trade and Industry unilateral authority to re-set domestic fuel prices on a monthly basis to pass through global oil prices to consumers without first seeking cabinet approval.

COMMENT

¶8. (C) An IMF balance of payments loan facility is absolutely the correct step for the GoE to address the persistent forex crisis and mitigate its dampening effects on growth. Embassy Addis Ababa strongly endorses this move on its own merits, but also due to the greater oversight role the loan effectively will grant to the IMF. We are concerned that despite the GoE's recognition that the current crisis is reflective of a structural problem, the GoE has yet to embrace a structural solution offering a longer-term solution. While the GoE itself acknowledges that promoting exports and foreign investment will not adequately address its external imbalance, there continues to be no willingness

to address the fundamental overvaluation of the Ethiopian Birr. As such, we strongly urge Washington agencies to support the IMF loan facility to the GoE. We further encourage them to take advantage of discussions on the matter to urge the Fund to press for GoE policy shifts to address the underlying structural problem either through reducing rigidities in the prevailing foreign exchange regime or opening the financial services sector to foreign parties to attract foreign investment at significantly greater levels.
End Comment.
MALAC